Huang Ee Hoe & Ors v Tiong Thai King & Ors

HIGH COURT (SIBU) — SUIT NO 54 OF 1984
CHONG SIEW FAI J
4 OCTOBER 1990

Companies and Corporations — Proceedings filed by shareholders — Whether shareholders proper plaintiffs — Exception to the rule in Foss v Harbottle — Derivative action — Application for preliminary issues to be tried — Whether prima facie case established by the plaintiffs — Whether company entitled to the reliefs sought — Proper time for determining preliminary issues

Civil Procedure — Preliminary issues — Disposing of preliminary issues before trial — Early disposal of preliminary issues placing parties in clearer position as to conduct of case

The first, second, third and fourth defendants took out a summons seeking an order for questions or issues to be tried and determined as preliminary questions or issues before the trial of the action. The plaintiffs were shareholders in the fifth defendant-company. The application sought an order to determine (a) whether the plaintiffs have established a prima facie case and are entitled to the reliefs claimed; (b) whether the plaintiffs are barred from bringing the action by the rule that the proper plaintiff in an action in respect of an alleged wrong done to the company is the company itself and not its shareholders; and (c) whether the plaintiffs fall within any exception to that rule on the basis of the matters disclosed in the amended statement of claim.

The plaintiffs objected to the application and submitted that the facts and law were closely and inseparably intertwined, that complex issues were involved, and that considerable details of fact including a question of fraud needed to be gone into which could only be done in a full trial. Furthermore, they contended that there was no independent board in the fifth defendant-company and that the company had not engaged any counsel nor taken any stand in the proceedings. Previous applications had also dealt with the two preliminary issues raised and therefore issue estoppel applied. The applicants, however, stated that the issues under the summons involved examination of the pleadings and that little evidence would be required.

Held, dismissing the plaintiffs' objections:

(1) The basic rule of law is that the only proper plaintiff in proceedings to redress a wrong against a company or to enforce a right of a company is the company itself. However, difficulties and injustice arose where the majority of the directors or shareholders were the wrongdoers or benefitted by the wrong because they would not sanction the bringing of actions by the company. To overcome the problem, exceptions to the rule have developed where minorities can bring a derivative action against the wrongdoers, joining also the company as a defendant.

(2) In a derivative action, before such an action is allowed to proceed, the defendants are entitled to ask for determination as a preliminary issue whether the plaintiffs have established a prima facie case (i) that the action falls within the proper boundaries of the exception to the rule in *Foss* v *Harbottle*,[2] and (ii) that the company is entitled to the relief claimed.

(3) What is required to be established is a prima facie case so as to avoid unjustifiably subjecting the company to a full trial in order to enable the court to determine whether the plaintiffs were entitled in law to make the company undergo the entire action. Trial of the preliminary issues is to this end.

(4) Leaving the preliminary issues to be dealt with at the commencement of the trial of the main action necessarily means that all are set for the trial including the subpoena and presence or attendances of witnesses of both sides. On the other hand, if the preliminary issues are disposed of in advance, preparatory works for the trial as aforesaid may or may not be necessary depending upon the result of the present application. An early disposal of the present application which would undoubtedly place parties in a clearer position as to whether anything needs to be done in the conduct of the case is to be preferred.

[Bahasa Malaysia summary

Defendan pertama, kedua, ketiga dan keempat mengeluarkan satu saman memohon satu perintah untuk soalan-soalan dan isu-isu dibicara dan diputuskan sebagai soalan atau isu permulaan sebelum perbicaraan tindakan itu. Plaintiff adalah pemegang saham di dalam syarikat defendan kelima. Permohonan itu memohon satu perintah untuk memutuskan (a) sama ada plaintif telah mendirikan satu kes prima facie dan berhak kepada relif yang dituntut; (b) sama ada plaintif disekat dari membawa tindakan itu oleh aturan bahawa plaintif yang betul di dalam tindakan berkenaan satu kesalahan yang didakwa telah dilakukan terhadap sebuah syarikat ialah syarikat itu sendiri dan bukan pemegang sahamnya; dan (c) sama ada plaintiff jatuh di dalam apa-apa kecualian kepada aturan itu atas dasar perkara yang dikemukakan di dalam pernyataan tuntutan yang dipinda.

Plaintif telah membantah terhadap permohonan itu dan menghujah bahawa fakta dan undang-undang tidak dapat dipisahkan, bahawa isu-isu yang susah terlibat, dan bahawa banyak perincian fakta termasuk satu soalan mengenai fraud mesti diperiksa dan ini hanya boleh dibuat di dalam satu perbicaraan penuh. Lagipun, mereka menghujah bahawa tidak ada lembaga yang bebas di dalam syarikat defendan kelima dan bahawa syarikat itu tidak mengupah sebarang peguambela atau mengambil sebarang pendirian di dalam prosiding itu. Permohonan sebelumnya telah memutuskan dua isu permulaan yang dibangkitkan dan oleh kerana itu estoppel isu terpakai. Pemohon, walau bagaimanapun, menyatakan bahawa isu-isu di dalam saman itu melibatkan pemeriksaan pliding dan bahawa keterangan yang sedikit akan diperlukan.

Diputuskan, menolak bantahan plaintif:

(1) Aturan dasar undang-undang ialah plaintif betul yang tunggal di dalam prosiding untuk memperbaiki satu kesalahan terhadap sebuah syarikat atau untuk menguatkuasakan satu hak syarikat itu ialah syarikat itu sendiri. Walau bagaimanapun, kesusahan dan ketidakadilan berbangkit apabila majoriti pengarah atau pemegang saham adalah orang yang berlaku salah atau mendapat keuntungan daripada kesalahan itu kerana mereka tidak akan meluluskan pembawaan tindakan oleh syarikat itu. Untuk mengatasi masalah itu, kecualian kepada aturan itu telah dimajukan di mana pihak minoriti boleh membawa satu tindakan derivatif terhadap orang yang berlaku salah, mencantum juga syarikat itu sebagai defendan.

(2) Di dalam satu tindakan derivatif, sebelum tindakan sedemikian dibenarkan berterusan, defendan berhak meminta pemutusan sebagai satu isu permulaan sama ada plaintif telah mendirikan satu kes prima facie (i) bahawa tindakan itu jatuh di dalam lingkungan yang berpatutan bagi kecualian kepada aturan di dalam *Foss* v *Harbottle*,[2] dan (ii) bahawa syarikat itu berhak mendapat relif yang dituntut.

(3) Apa yang perlu didirikan adalah satu kes prima facie supaya mengelak daripada mendedahkan syarikat itu secara tidak wajar kepada satu perbicaraan penuh untuk mahkamah memutuskan sama ada plaintiff berhak di sisi undang-undang membuat syarikat itu melalui seluruh tindakan itu. Perbicaraan isu permulaan adalah untuk tujuan ini.

(4) Meninggalkan isu permulaan untuk diperiksa di permulaan perbicaraan tindakan utama mesti bermakna bahawa semua telah disediakan untuk perbicaraan termasuk sepina dan kehadiran saksi kedua-dua pihak. Sebaliknya, jika isu permulaan diputuskan terdahulu, usaha persediaan untuk perbicaraan seperti yang telah disebut mungkin perlu atau tidak perlu bergantung kepada keputusan permohonan ini. Pemutusan awal permohonan ini yang sudah barang tentu akan meletakkan pihak-pihak yang berkenaan dalam kedudukan yang lebih jelas tentang sama ada apa-apa perlu dibuat dalam menjalankan kes ini adalah lebih baik.]

Cases referred to

1 *Prudential Assurance Co Ltd* v *Newman Industries Ltd & Ors (No 2)* [1982] 1 All ER 354 (folld)
2 *Foss* v *Harbottle* (1843) 2 Hare 461; 67 ER 189 (folld)
3 *Burland* v *Earle* [1902] AC 83 (folld)
4 *Paidiah Genganaidu* v *The Lower Perak Syndicate Sdn Bhd & Ors* [1974] 1 MLJ 220 (folld)
5 *Smith* v *Croft (No 2)* [1987] 3 All ER 909 (refd)
6 *Tilling* v *Whiteman* [1979] 1 All ER 737 (distd)
7 *Chan Kum Loong* v *Hii Sui Eng* [1980] 1 MLJ 313 (distd)
8 *Carl-Zeiss-Stiftung* v *Herbert Smith* [1968] 2 All ER 1002 (folld)

George Lo for the plaintiffs.
HC Sim for the defendants.

Cur Adv Vult

Chong Siew Fai J: By a summons dated 1 March 1990 the applicants, ie the first, second, third and fourth defendants (collectively called 'the defendants') seek for an order that:

(i) the following questions or issues raised in para 2(ii) of the defence and para 1 of the reply to defence be tried and determined as preliminary questions or issues before all other questions and issues in this action, namely:

  (a) whether the plaintiffs have established a prima facie case that Sarawak Building Supplies Sdn Bhd ('the company') is entitled to the reliefs claimed in the amended writ of summons and the amended statement of claim filed herein?
  (b) whether the plaintiffs are barred from bringing this action by the rule that the proper plaintiffs in an action in respect of an alleged wrong done to the company is the company itself and not its shareholders? and
  (c) whether the plaintiffs fall within any exceptions to that rule on the basis of the matters disclosed in the amended statement of claim?

(ii) that such directions as this honourable court may deem fit, be given for the trial or determination of the said preliminary questions or issues; and

(iii) that the costs of and occasioned by this application be costs in the action.

Since the issue of the summons, the defence has been amended. However, para 2(ii) of the defence mentioned in item (i) of the relief sought remains unchanged. Paragraph 2(ii) reads:

> The first, second, third and fourth defendants (hereinafter collectively referred to as 'the defendants') deny that the plaintiffs were and are legally entitled to maintain this action or at all.

Paragraph 1 of the plaintiffs' reply pleads:

> As regards para 2(ii) of the defence, the first and the second plaintiffs will say that they are legally entitled to sue the defendants, including the fifth defendant, in the nature of a derivative action for and on behalf of themselves and for and on behalf of the other 'B' shareholders of the fifth defendant-company. The ruling of the honourable court dated 15 December 1988 is pertinent.

Relying on *Prudential Assurance Co Ltd* v *Newman Industries Ltd & Ors (No 2)*,[1] the defendants through Mr Fong wished the issues framed to be determined.

For the plaintiffs, Mr Lo objected to the application on grounds which I shall deal in a moment.

The basic rule of the law is that the only proper plaintiff in proceedings to redress a wrong against a company or to enforce a right of a company is the company itself. (*Foss* v *Harbottle*;[2] *Burland* v *Earle*[3] at p 93; *Paidiah Genganaidu* v *The Lower Perak Syndicate Sdn Bhd & Ors.*[4]) This rule has come to be known as the rule in *Foss* v *Harbottle.*[2] However, difficulties and injustice arose where the majority of the directors or shareholders were the wrongdoers or benefitted by the wrong because they would not sanction the bringing of actions by the company. To overcome the problem, exceptions to the rule have developed where minorities can bring a 'derivative action' (a term originated in the United States) on behalf of themselves and all the other shareholders (except the wrongdoer) against the wrongdoers, joining also the company as a defendant. One of such exceptions is where there is allegedly fraud on the minority and the wrongdoers are in control of the company (*Burland* v *Earle*[3] at p 93).

Prudential Assurance Co Ltd v *Newman Industries Ltd & Ors (No 2)*[1] relied on by the plaintiffs was a derivative action. It appears clear from that case that before such an action is allowed to proceed, the defendants are entitled to ask for determination as a preliminary issue whether the plaintiffs have established a prima facie case:

(i) that the action falls within the proper boundaries of the exception to the rule in *Foss* v *Harbottle;*[2] and
(ii) that the company is entitled to the relief claimed.

The relevant part of the judgment (at pp 365-366) on the point and the reasoning therefor are reproduced below:

... We desire however to say two things. First, as we have already said, we have no doubt whatever that the judge erred in dismissing the summons of 10 May 1979. He ought to have determined as a preliminary issue whether the plaintiffs were entitled to sue on behalf of Newman by bringing a derivative action. It cannot have been right to have subjected the company to a 30-day action (as it was then estimated to be) in order to enable him to decide whether the plaintiffs were entitled in law to subject the company to a 30-day action. Such an approach defeats the whole purpose of the rule in *Foss* v *Harbottle* and sanctions the very mischief that the rule is designed to prevent. By the time a derivative action is concluded, the rule in *Foss* v *Harbottle* can have little, if any, role to play. Either the wrong is proved, thereby establishing conclusively the rights of the company, or the wrong is not proved, so cadit quaestio. ...

... The second observation which we wish to make is merely a comment on the judge's decision that there is an exception to the rule in *Foss* v *Harbottle* whenever the justice of the case so requires. We are not convinced that this is a practical test, particularly if it involves a full-dress trial before the test is applied. On the other hand we do not think that the right to bring a derivative action should be decided as a preliminary issue on the hypothesis that all the allegations in the statement of claim of 'fraud' and 'control' are facts, as they would be on the trial of a preliminary point of law. In our view, whatever may be the properly defined boundaries of the exception to the rule, the plaintiff ought at least to be required before proceeding with his action to establish a prima facie case (i) that the company is entitled to the relief claimed and (ii) that the action falls within the proper boundaries of the exception to the rule in *Foss* v *Harbottle.*

It should perhaps be noted that the observation on procedure in the judgment quoted above is clearly obiter because when the Court of Appeal (English) made the pronouncement, the whole action had been heard and determined and, also, the company, Newman Industries Ltd had intended to accept the decision on the case made in its favour with the result that the question of whether the plaintiff was entitled to bring the derivative action was no longer relevant. On the other hand, the procedure was adopted and similar issues considered in subsequent derivative actions. See, eg *Smith* v *Croft (No 2).*[5]

Though conceding that *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] is a persuasive authority, counsel for the plaintiffs/respondents, in the attempt to dissuade me from following it, submitted that the facts and the law in our instant case were closely and inseparably interwined, that complex issues were involved, and that considerable details of fact including question of fraud needed to be gone into which could only be done in a full trial. For the applicants, Mr Fong stated that the issues under the summons involved examination of pleadings on which he would solely rely and that little evidence would be required. As regards the voluminous documents reflected in the list of documents filed under the discovery, he pointed out that they largely consisted of invoices and log lists.

It is necessary to bear in mind that what was stated to be required in *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] respecting the two issues in question is that *a prima facie case* be made out. The reasoning for such a course is, as explained in the *Prudential Assurance* case,[1] to avoid unjustifiably subjecting the company to a full trial in order to enable the court to determine whether the plaintiffs were entitled in law to make the company undergoing the entire action.

The observations about trials of preliminary issues of law and fact expressed in *Tilling v Whiteman*[6] and *Chan Kum Loong* v *Hii Sui Eng*[7] are, in my opinion, inapplicable in our instant case. The two cases are not derivative actions. The question of exception to the rule of *Foss* v *Harbottle* does not arise. It appears to me that the inference to be drawn from *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] is that a derivative action is unlikely to be allowed to go on unless the plaintiffs show a prima facie case of entitlement to the relief claimed and of control of the company by the alleged wrongdoers, who are using their controlling power to prevent the action from being brought by the company. Trial of the preliminary issues is to this end.

Next, it was contended for the plaintiffs/respondents that *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] was distinguishable in that, unlike that case, there was no independent board in our case, that the fifth defendant-company, Sarawak Building Supplies Sdn Bhd, did not engage any counsel and had not assumed the position that the advantageous outcome of the suit would be 'vastly outweighed by harm inflicted upon it by the action ...', and that, consequently, this court need not and should not consider the question: 'Ought I to be trying a derivative action?'

I find no merits in the contentions. Where there are independent directors or shareholders, it is implicit from the judgment in *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] that their views are weighty and important. But where, as it appears in our instant case, an independent component is lacking, the court nevertheless has to deal with the preliminary issues, if raised, by considering the standpoints of the directors or shareholders of both sides.

Mr Lo, I noted, pointed to the outcome of a shareholders' meeting held on the direction of the court. That would be a matter for consideration in the hearing of the substantive application.

For the plaintiffs/respondents it was further argued that issue estoppel applied to the two preliminary issues raised in that they had been dealt with at the hearing of previous applications. I have gone through the matters raised in the previous proceedings. In this respect, I agree with Mr Fong of counsel for the applicants and I have no doubt that the issues contained in the present

summons had not been decided. A clear indication of that may be seen in my ruling on 15 December 1988, particularly pp 3-4 thereof.

The application should, in my view, be allowed to proceed subject, however, to the modifications stated below. The modifications are in keeping with the obiter dictum in *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*[1] at p 366 upon which the applicants heavily, and, I would say, solely rely for this application. Furthermore, the issues suggested in the *Prudential Assurance* case[1] are not pure questions of law. Facts are necessarily involved. Having regard to O 33 r 2 relied on by the defendants/applicants which also empowers the court to direct the manner in which a question is to be stated, and adhering as best as possibly could to the applicants' original framing of the issues bearing in mind, at the same time, the guidance in *Prudential Assurance Co Ltd* v *Newman Industries Ltd (No 2)*,[1] I would order the following modifications to the issues appearing in the summons:

(i) delete the last word 'and' appearing in prayer (i) (b) of the summons, and substitute therefor the word 'or', and

(ii) delete the words 'on the basis of the matters disclosed in the amended statement of claim?' and substitute therefor the words: 'which permits minority shareholders to bring an action, in other words, within any exceptions to the rule in *Foss* v *Harbottle*'.

After modification, prayers (i)(b) and (c) read thus:

> (b) whether the plaintiffs are barred from bringing this action by the rule that the proper plaintiffs in an action in respect of an alleged wrong done to the company is the company itself and not its shareholders? or
>
> (c) whether the plaintiffs fall within any exceptions to that rule which permits minority shareholders to bring an action, in other words, within any exceptions to the rule in *Foss* v *Harbottle*.

The applicants, in my view, are not in any way prejudiced by the alteration to prayer (i) (c) for it seems to me that any attempt sought to have the action dismissed or struck out by reason of any alleged defective pleading may be made under the applicants' summons dated 3 July 1984 which, as the proceedings in this action indicate, the applicants have every intention to pursue.

Finally, for the plaintiffs/respondents, it was urged upon me that if the application were to be allowed, the preliminary issues be dealt with at the commencement of the trial of this action. I am unable to accept this. Leaving the issues for disposal at the commencement of trial of the main action necessarily means that all are set for the trial including the subpoena and presence or attendances of witnesses of both sides in participation of the trial to proceed. On the other hand, if the preliminary issues are disposed of in advance, preparatory works for the trial as aforesaid may or may not be necessary dependent upon the result of the present application. An early disposal of the present application would undoubtedly place parties in a clearer position as to whether anything needs be done in the conduct of the case, and is, in my opinion, to be preferred.

As stated by Lord Denning MR in *Carl-Zeiss-Stiftung* v *Herbert Smith*[8] at p 1004:

> The true rule was stated by Romer LJ in *Everett* v *Ribbands* [1952] 2 QB 198
>
> Where there is a point of law which, if decided in one way, is going to be decisive of the litigation, advantage ought to be taken of the facilities afforded by the rules of court to have it disposed of at the close of pleadings or very shortly afterwards.
>
> I have always understood such to be the practice.

Romer LJ, of course, was referring to issue of point of law. The observation on timing, in my opinion, equally applies to the issues raised and modified in the present summons.

Except for the formal adjournment on 14 May 1990, costs hitherto incurred in the hearing of this summons be reserved.

Quite detached from the present application, Mr Lo, in the course of his submission, had asked for early hearing of the applicants' summons dated 10 May 1990 applying for an earlier trial of this action. I suggest that the request be made to the senior assistant registrar. However, in view of the nature of the relief sought in the application presently under consideration, there ought, I trust, be no objection that the said summons be heard after the disposal of the issues earlier on stated herein.

Objections dismissed.

Solicitors: *Nashir Johal & Co; Reddi & Co.*

Reported by *Yap Shao Sin*